

PRI Reporting Framework 2013 Main definitions

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UNEP Finance Initiative
Innovative financing for sustainability



United Nations Global Compact

An investor initiative in partnership with UNEP Finance Initiative and UN Global Compact

Table of Contents

Introduction	3
ESG issues	4
Active/ Passive investments	5
ESG incorporation	6
Active ownership and engagement	9

Introduction

This document presents some of the main and most frequently used definitions in the PRI Reporting Framework. These definitions are presented here as their use is either frequent and/or key for preparing to report, as well as to understand the reported information by other signatories. In the offline version of the Reporting Framework, you will not find these definitions repeated in each indicator, so it is key that you look at these general definitions here.

ESG issues

Definition	ENVIRONMENT, SOCIAL AND GOVERNANCE ISSUES
<p>A definitive list of environmental, social and governance (ESG) issues does not exist. It would not be possible or desirable to produce a list, or a set of definitions, that claimed to be exhaustive or definitive. Any such list would inevitably be incomplete and would soon be out of date.</p> <p>Nonetheless, the table below provides examples of ESG issues, for guidance purposes. This is intended primarily for signatories who are relatively new to responsible investment and to the PRI. Some modules (e.g. Property) provides examples of ESG issues that are specific to that sector or asset class.</p>	
<p>Environmental (E)</p>	<p>Issues relating to the quality and functioning of the natural environment and natural systems. These include: biodiversity loss; greenhouse gas (GHG) emissions, climate change, renewable energy, energy efficiency, air, water or resource depletion or pollution; waste management; stratospheric ozone depletion; changes in land use; ocean acidification and changes to the nitrogen and phosphorus cycles.</p>
<p>Social (S)</p>	<p>Issues relating to the rights, well-being and interests of people and communities. These include: human rights, labour standards in the supply chain, child, slave and bonded labour, workplace health and safety, freedom of association and freedom of expression, human capital management and employee relations; diversity; relations with local communities, activities in conflict zones, health and access to medicine, HIV/AIDS, consumer protection; and controversial weapons.</p>
<p>Governance (G)</p>	<p>Issues relating to the governance of companies and other investee entities. In the listed equity context these include: board structure, size, diversity, skills and independence; executive pay; shareholder rights; stakeholder interaction; disclosure of information; business ethics; bribery and corruption; internal controls and risk management; and, in general, issues dealing with the relationship between a company's management, its board, its shareholders and its other stakeholders. This category may also include matters of business strategy, encompassing both the implications of business strategy for environmental and social issues, and how the strategy is to be implemented.</p> <p>In the unlisted asset classes governance issues also include matters of fund governance, such as the powers of Advisory Committees, valuation issues, fee structures, etc.</p>
<p>Numerous organisations and projects have identified ESG issues by sector, together with associated key performance indicators. Examples include:</p> <ul style="list-style-type: none"> • The European Federation of Financial Analysts Societies (EFFAS): KPIs for ESG - A Guideline for the Integration of ESG into Financial Analysis and Corporate Valuation • The CFA Institute: Environmental, Social and Governance Factors at Listed Companies - A Manual for Investors • UNEP FI and WBCSD: Translating environmental, social and governance factors into business value <p>ESG research providers and brokers are also well placed to provide advice in this area.</p>	

Active/ Passive investments

Definition	ACTIVELY AND PASSIVELY MANAGED STRATEGIES
Passive strategies	Investment strategies or funds that aim to replicate broad capital market index benchmarks (for this reason they are referred to as index or tracker funds).
Active - quantitative (quant) strategies	Investment strategies or funds where the manager builds computer-based models to determine whether an investment is attractive. In a pure "quant model" the final decision to buy or sell is made by the model.
Active - fundamental	Fundamental strategies in which investment decisions are based on human judgment. This includes both bottom-up (e.g. stock-picking) and top-down (e.g. sector-based) strategies.
Active - other	Strategies that do not match any of the above strategies. These may be active strategies that combine active quant and active fundamental strategies, or other strategies that you believe do not fit at all the above definitions. You may clarify your strategy in Additional Information field.

ESG incorporation

Definition	ESG INCORPORATION
<p>Incorporation of ESG issues into investment analysis and decision-making processes is covered in Principle 1 of the PRI.</p> <p>Throughout the Reporting Framework, we refer to ESG incorporation as <i>the review and use of ESG information in the investment decision-making process</i>. The Reporting Framework addresses four ways in which this can be done:</p> <ul style="list-style-type: none"> • Screening • Sustainability themed investment (also referred to as environmentally and socially themed investment) • Integration of ESG issues • A combination of the above <p>Assets subject to an engagement approach only and not subject to any of the above strategies should not be included in ESG incorporation.</p> <p>To improve standardisation and communication in the responsible investment industry, the PRI is aligning its definitions with those of the Global Sustainable Investment Alliance. These are presented below for convenience.</p>	
Screening of investments	<p>This involves three types of screening:</p> <ol style="list-style-type: none"> a. Negative/exclusionary screening: The exclusion from a fund or portfolio of certain sectors, companies or practices based on specific ESG criteria; b. Positive/best-in-class screening: Investment in sectors, companies or projects selected for positive ESG performance relative to industry peers; c. Norms-based screening: Screening of investments against minimum standards of business practice based on international norms.
Sustainability themed investing	Investment in themes or assets specifically related to sustainability (for example clean energy, green technology or sustainable agriculture).
Integration of ESG issues	The systematic and explicit inclusion by investment managers of environmental, social and governance factors into traditional financial analysis.
<p>Investment decision-making processes</p> <p>For the purposes of the Reporting Framework, <i>investment decision making processes</i> refers to research, analysis and other processes that lead to a decision to make or retain an investment (i.e. to buy, sell or hold a security), or to commit capital to an unlisted fund or other asset.</p> <p>(Proxy) voting decisions and engagement activities are not classified as investment decisions for the purposes of the Reporting Framework. These decisions fall under Principle 2 of the PRI, relating to active ownership, and within the <i>Listed Equity – Active Ownership (LEA)</i> module of the Framework.</p>	

FURTHER EXPLANATION OF DEFINITIONS FOR ACTIVE STRATEGIES

<p>Screening</p>	<p>Screening covers both screening conducted under a manager’s own policy and client-directed screening.</p> <p>Negative/exclusionary screening and positive/best-in-class screening are based on criteria defined in a variety of ways: by product, activity, sector, geographic region or management practices.</p> <p>Norms-based screening involves either: i) defining the investment universe based on investees’ performance on international norms related to responsible investment/ESG issues, or ii) excluding investees from portfolios after investment if they are found following research, and sometimes engagement, to contravene these norms. Such norms include but are not limited to the UN Global Compact Principles, the Universal Declaration of Human Rights, International Labour Organization standards, the United Nations Convention Against Corruption and the OECD Guidelines for Multinational Enterprises.</p>
<p>Sustainability themed investing</p>	<p>Sustainability themed investing involves the selection of assets that contribute to addressing sustainability challenges such as climate change or water scarcity. Funds can either be single-themed or multi-themed. For the purpose of this Reporting Framework, we use interchangeably the term environmental and social themed and sustainability themed investments.</p>
<p>Integration of ESG issues</p>	<p>Integration of ESG issues encompasses the use of qualitative and quantitative ESG information in investment processes, with the objective of enhancing investment decision-making. Integration of ESG issues can be used to inform economic analysis and industry analysis. It can be used at the portfolio level, by taking into account ESG-related trends such as climate change, or at the stock, issuer, or investee level. The term is used interchangeably with ESG integration or integrated analysis.</p> <p>Integrated analysis for active stock-picking or other equity investments includes analysing how ESG issues can affect a company’s balance sheet, income statement or cash flow models, by affecting costs, revenues, and business growth assumptions (i.e. in the estimation of a company’s fundamental value). Integrated analysis for active bond-picking and other debt funds involves analysing how ESG issues can affect an issuer’s creditworthiness. This type of analysis can also be used by funds that pick bond issuers using quantitative modelling. Integrated analysis for both equities and debt includes an assessment of a company’s quality of management and the business risks and opportunities it faces related to ESG issues, allowing comparisons between companies.</p> <p>For examples of how investors are conducting integrated analysis for listed equities, see Integrated Analysis: How Investors Are Addressing Environmental, Social and Governance Factors in Fundamental Equity Valuation, published by the PRI in February 2013.</p>
<p>Combined approaches</p>	<p>Combined approaches might include for example:</p> <ul style="list-style-type: none"> • Establishing a sustainable agriculture thematic fund that screens out companies involved in producing tobacco and uses integrated analysis to select companies for inclusion in the fund. • Running a fund that applies 20 negative screens to determine the investible universe and uses integrated analysis to select companies for investment from within the investible universe. • Running a global equities fund using integrated analysis to select stocks combined with a norms-based approach, investigating any serious alleged breaches of selected international norms and divesting companies found to be in serious breach of a norm (often after engagement).

FURTHER EXPLANATION OF DEFINITIONS FOR PASSIVE STRATEGIES

<p>Screening</p>	<p>Screening may include the use of indices constructed from an eligible universe based on the ESG characteristics of a company or country, but in which ESG issues do not play a part in the weighting of those companies or countries within the index. This may include indices constructed using ESG best-in-class or positive selection methodologies which identify securities for index inclusion (e.g. FTSE4Good, Dow Jones sustainability and MSCI ESG indices) or indices that exclude particular companies or countries (e.g. on the basis of products or activities). Exclusions may also be activity-based (i.e. exclude securities on the basis of their industry or business activities, for example, tobacco or controversial weapon screens), or location-based (i.e. exclude securities from companies who operate in certain countries, or the sovereign debt from those countries). Alternatively, there may be norms-based exclusions (i.e. indices which exclude securities of issuers considered to have broken certain minimum standards of business conduct based on international norms, such as the UN Global Compact).</p>
<p>Sustainability themed investments</p>	<p>Sustainability themed investments cover passive funds investing in companies linked to specific themes (e.g. indices focused entirely on environmental and social themes such as clean technology, climate change, microfinance and impact investing).</p>
<p>Integration of ESG issues</p>	<p>Integration of ESG issues typically alternative weighted ESG indices in which constituent security weights take account of the ESG characteristics of the company or country.</p>

Active ownership and engagement

Definition	ACTIVE OWNERSHIP AND ENGAGEMENT
Active ownership	Active ownership is the use of the rights and position of ownership to influence the activity or behaviour of investees. This can be applied differently in each asset class. For listed equities it includes both engagement and (proxy) voting (including filing shareholder resolutions). For other asset classes (e.g. fixed income), engagement may still be relevant while (proxy) voting may not.
Engagement	Engagement refers to interactions between the investor and current or potential investees (which may be companies, governments, municipalities, etc.) on ESG issues. Engagements are undertaken to influence (or identify the need to influence) ESG practices and/or improve ESG disclosure.
(Proxy) voting and shareholder resolutions	Voting refers to voting on management and/or shareholder resolutions as well as filing shareholder resolutions.

FURTHER EXPLANATION OF DEFINITIONS FOR ENGAGEMENT

Do not include the following as engagements:

- Interactions with companies for data collection and/or research purposes related to buy/hold/sell/weight decisions.
- Standard questionnaires sent to companies for the purposes of information gathering and investment decision-making related to Principle 1 only (e.g. on products, or ESG policies and performance, for screening purposes).
- Attendance at a company presentation, AGM or other company meeting without interactions or discussion.
- CDP's disclosure requests on GHG emissions, water and forests. These are not captured as engagements but are reported in Overarching Approach (OA).
- Press releases an investor may publish regarding a practice an investee is undertaking which the investor is aiming to change.

Interactions intended to influence public policy or industry bodies defining best practices may not necessarily relate to specific underlying assets. Hence, do not report these in the asset class modules, but in the Overarching Approach (OA) module.

ENGAGEMENTS SPLIT BY WHO CONDUCTS THEM

There are many different configurations of engagement. Investors engage with companies directly in their own name, in collaboration with other investors (through investor networks and membership organisations) and through commercial service providers. The distinctions between these are not always clear-cut. Please use the definitions below and your best professional judgement when deciding how to classify your engagement. Review the process indicators for each category (LEA 03-04 for internal; LEA 05-06 for collaborative; and LEA 07-08 for service providers) and determine which indicator/s best fit your business model.

Please contact the Reporting and Assessment team if you require additional clarification.

<p>Individual/ Internal staff engagement</p>	<p>The defining characteristics of an individual/internal staff engagement are:</p> <ul style="list-style-type: none"> • it is carried out by your internal staff alone, with no involvement or support from other investors, investor networks or service provider • it is conducted in the name of your organisation (i.e. the companies with which you engage can identify your organisation individually) and you do not act on behalf of other organisations. <p>Joining the CDP should not be counted as an engagement but reported as part of the way you support responsible investment in Organisational Approach OA10. However, if your organisation engages in its own name with companies on their carbon emissions, water or forest footprint disclosure as a follow-up to CDP disclosure requests, you should report these engagements as individual/internal staff engagements.</p>
<p>Collaborative engagement</p>	<p>Collaborative engagement is engagement that an investor conducts jointly with other investors. This includes:</p> <ul style="list-style-type: none"> • groups of investors working together without the involvement of a formal investor network or other membership organisation. • groups of investors working together with the support of a formal investor network or other membership organisation, with some level of support but with individual members of the collaboration responsible for most of the engagement activity. • collaborative engagement supported by PRI staff and conducted through the PRI Clearinghouse platform. <p>Joining the CDP should not be counted as an engagement but reported as part of the way you support responsible investment in Organisational Approach OA10. However, if your organisation engages with a group of investors in its own name with companies on their carbon emissions, water or forest footprint disclosure as a follow-up to CDP disclosure requests, you should report these engagements as collaborative engagements.</p>
<p>Service provider engagement</p>	<p>Service provider engagements include engagements conducted via:</p> <ul style="list-style-type: none"> • commercial parties that provide stand-alone engagement services, without managing their clients' underlying assets. • investor organisations that conduct engagement on their members' behalf, and which have an explicit mandate from their members to represent them. <p>These include engagements conducted entirely on an outsourced basis as well as those facilitated by the service provider but the investor's own staff undertake some of the engagement activity.</p>

ENGAGEMENT INTENSITY AND EFFORT

Investors interact with companies and issuers at different levels of intensity and effort. The levels of intensity and effort are defined below.

Definition	ENGAGEMENT INTENSITY
<p>Comprehensive engagement</p> <p>(for collaborative and service provider engagements)</p>	<p>A comprehensive engagement includes multiple, substantive, detailed discussions or interactions with a company (e.g. letters, meetings and calls) relating to a particular ESG issue.</p>

Definition	ENGAGEMENT EFFORT
<p>Leading role</p> <p>(for collaborative engagements)</p>	<p>Defined as writing and/or following up on joint letters, regularly joining group conference calls, leading dialogue with companies, participating in some meetings with companies organised by other investors, and sharing relevant information on the topic and companies with other members of the collaboration.</p>
<p>High involvement engagements</p> <p>(for service provider engagements)</p>	<p>Defined as situations where you:</p> <ul style="list-style-type: none"> • spend significant time and effort setting goals and objectives for specific engagements and monitor them proactively; and/or, • wrote or followed up on joint letters with the service provider (possibly alongside other investors); and/or, • regularly joined group conference calls; and/or, • participated in some meetings with companies organised by the service provider.